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An Overview of the Rental Market in the

Sioux Falls, South Dakota
Metropolitan Statistical Area (MSA)

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The Sioux Falls, South Dakota MSA Rental Market

Introduction

This report has been prepared to assist the U.S. Department of Housing and Urban Development (HUD) in its underwriting operations. It has also been provided to officials of state and local government, developers, lenders and others interested in the outlook for the local rental market. The estimates, opinions and forecasts in this report are solely those of the Economists in the Office of Policy Development and Research in the Rocky Mountain Office and do not represent HUD Departmental or Rocky Mountain Office policy. This report is provided for informational purposes only. It does not purport to make determinations with respect to any particular application for mortgage insurance, subsidy funds, grants or other financing that may be under consideration in this market area.

The market area covered by this analysis consists of the Sioux Falls Metropolitan Statistical Area (MSA), which is defined as Minnehaha and Lincoln Counties, South Dakota. The report includes a discussion of the condition and outlook for the overall rental market and the market for income restricted projects financed under the Low Income Housing Tax Credit (LIHTC) program, including projects which provide income restricted units as a result of obtaining financing through issuance of tax exempt, Private Activity Bonds (PABs). It does not address specialized portions of the rental market such as congregate elderly housing or assisted living but it does include a brief review of the outlook for independent LIHTC units reserved for seniors. The analysis does include a brief discussion of the home sales market. Unless otherwise noted, the estimates and discussion of market conditions are as of July 2001.

Summary and Conclusions

Sioux Falls' employment experienced strong growth during the 1990s but by late 2000, growth began to slow because of layoffs in the computer industry. Consequently, average employment during the 6-month period ending in June 2001 was 1.2 percent above the level recorded during the same period a year ago, well below the 3.8 percent annual average growth rate of the 1990s. Despite the slowdown, the unemployment rate in June was 1.6 percent, only slightly above the rate from a year ago. The outlook over the next few years is for some modest increase in the growth rate, but not a return to the high rates recorded during the 1990s. Population increased at a relatively steady 2 percent a year since 1990, reaching an estimated 177,000 persons as of July 2001. Approximately 70 percent of the MSA's population resides in the city of Sioux Falls.

The rental market remains balanced despite a large number of units coming on line this year. The overall vacancy rate increased to 4.8 percent from the 3.4 percent recorded a year earlier. Although the vacancy rate is up, slight rent increases continue throughout the market. A cutback in apartment construction from 1997 to 1999, coupled with the inflow of new worker households migrating to the area, tightened the market. As the rental market improved, another construction spike occurred in 2000, with many new units coming on line during the first half of this year. Given the slower economy, builders are waiting to see how the market stabilizes following the absorption of these units before starting additional projects. Multifamily permit activity is down by over 70 percent during the first six months of this year and few starts are planned in the second half of this year. Demand for new rental units is estimated at 400 units in 2002 and 500 units in 2003. The higher number of units in the second year reflects the anticipated increase in employment growth. The nearly 250 units currently under construction are below the expected annual absorption level. The market should remained balanced during the second half of 2001 and begin to tighten by the first half of 2002.

The LIHTC rental market has recovered from some easing following a surge in production in the mid-1990s. The vast majority of the area's 1,220 LIHTC units are for households with incomes less than 60 percent of the median, but rents are typically $100 to $150 below the maximum allowable under the tax credit program and well below the area's Section 8 Fair Market Rents (FMRs). Section 8 voucher holders occupy approximately 40 percent of the nonelderly tax credit units in Sioux Falls. Even after adjusting for occupancy by the Section 8 voucher holders, the combined capture rates for 50 and 60 percent two and three bedroom units are close to limits observed in other market areas. The continued use of Section 8 vouchers to occupy additional LIHTC units will be limited because the number of vouchers is limited. Therefore, future development should be encouraged in other income levels and unit sizes. Because there has been no production of 40 percent units, there is strong need for all bedroom types below this income level. One and four bedroom units are in short supply for 50 and 60 percent income levels. There is also a strong need for elderly LIHTC units, where there has been little production. Under HUD's Section 8 program, there is a substantial unmet need among both elderly and family households eligible for rental assistance.

Employment Trend

Sioux Falls is the commercial, industrial and financial center of the state, and regional trade and service center for much of southeastern South Dakota. Historically, agriculture and meatpacking were the mainstays of the economy, but recent growth in computer manufacturing, financial and medical services, and the retail sector have helped diversify the economy. Private sector employers with over one thousand employees are Sioux Valley Hospital, Citibank (South Dakota) NA, John Morrell & Company, Avera McKennan Hospital, Gateway, Inc., Midwest Coast Transport, Hy-Vee Food Stores, Norwest Bank South Dakota NA, Hutchinson Technology and Specialized Card Services.

The economy maintained strong job gains throughout the 1990s; average annual wage and salary employment growth was 3.8 percent a year. Strongest growth was recorded in the services, finance and trade industrial sectors, which account for over 70 percent of the total job gain since 1990. Low operating costs, absence of state corporate income taxes and an available labor supply have helped the area attract businesses and jobs. The city's close proximity to the two state universities, coupled with the continued inflow of workers from rural areas, has helped supply the labor force to accommodate the recent job growth. This has allowed Sioux Falls to simultaneously maintain job growth, while having one of the lowest unemployment rates in the country.

The recent trend in civilian unemployment rate and wage and salary employment for the MSA is presented in the following table:

Table 1

Unemployment Rate and Wage and Salary Employment
Sioux Falls, South Dakota MSA
1990 - 2001

Year	Unemployment rate	Wage and salary employment Number	Change
1990	2.8%	79,300	na
1991	2.5%	82,500	4.0%
1992	2.4%	86,000	4.2%
1993	2.5%	88,800	3.3%
1994	2.4%	92,300	3.9%
1995	2.0%	96,000	4.0%
1996	2.1%	99,000	3.1%
1997	2.0%	102,100	3.1%
1998	1.7%	106,100	3.9%
1999	1.8%	111,600	5.3%
2000	1.5%	114,700	2.6%
June 2000(a)	1.6%	114,100	na
June 2001(a)	1.7%	115,400	1.2%

(a) 6-month period ending June.

Source: South Dakota Department of Labor

The economy slowed over the past year from the rapid growth of the 1990s because of a general weakness in the U.S. computer industry. Poorer demand for computers forced several hundred layoffs at Hutchinson Technology and Gateway computer; the primary factor in the lower employment growth rate (1.2 percent) through June of this year. Surprisingly, the average unemployment rate increased only slightly to 1.7 percent (1.6 percent was recorded in June 2000). Sioux Falls' unemployment rate has been below 3 percent since 1990 and below 2 percent since 1997. The average annual wage in the Sioux Falls MSA (Minnehaha and Lincoln Counties) during

2000 was $27,739, above all but one of South Dakota's 66 counties and above the state average of $24,803.

Overall, employment growth should begin to increase to the 2.5 to 3 percent range over the next few years, up from this year but below the stronger growth of the 1990s. Planned expansions by existing manufacturing firms, a stabilized local high technology sector and the city's continued growth in trade and services should help the economy bounce back from its current slowdown. A return to the high growth rates of the 1990s, over the short term, is not expected because of slowing in-migration and a sluggish U.S. economy.

Population Trend

Population growth in the Sioux Falls MSA paralleled the steady employment growth of the 1990s (see table 2). In-migration accounted for over 60 percent of the population gain over the past decade. This trend will likely persist over the next few years given the expected increase in employment growth, although in-migration will slow from the past few years. The current estimated population for the MSA is about 177,000 persons as of July 1, 2001, a 2.4 percent annual average increase from July 1 of last year. This is above the decade annual average of 2.1 percent. As mentioned above, this population movement from the rural areas of South Dakota will likely continue in 2002 and 2003 and the economy is expected to improve. Employment growth of 2.75 percent in 2002 and 3 percent in 2002 should result in population increasing to 185,200 persons by 2003. Population and migration trends are presented in the following table:

Table 2

Population and Components of Change
Sioux Falls, South Dakota MSA
1990 - 2001

Date	Population (a)	Net natural increase (b)	Migration (a)	Population change Number	Population change Percent
July 1990	139,800	na	na	na	na
July 1991	142,600	1,300	1,500	2,800	2.0%
July 1992	146,600	1,300	2,700	4,000	2.8%
July 1993	149,800	1,100	2,100	3,200	2.2%
July 1994	153,800	1,200	2,800	4,000	2.7%
July 1995	156,300	1,100	1,400	2,500	1.6%
July 1996	159,500	1,200	2,000	3,200	2.0%
July 1997	160,900	1,300	100	1,400	0.9%
July 1998	163,700	1,200	1,600	2,800	1.7%
July 1999	168,300	1,200	3,400	4,600	2.8%
July 2000	172,800	1,400	3,100	4,500	2.7%
July 2001	177,000	1,400	2,800	4,200	2.4%

Note: All numbers rounded to nearest one hundred.

(a) Population and migration estimates adjusted by HUD Economist to be consistent with the 2000 census.
(b) Excess of resident births over deaths in prior year.

Source: U.S. Census Bureau; South Dakota Department of Health; HUD Economist.

Housing Inventory

The housing inventory in the MSA expanded by nearly 13,800 units in the 1990s. These additions, coupled with a small increase in vacancies, resulted in a net gain of over 13,600 households. The following table compares the inventory, tenure and vacancy data from the 1990 and 2000 Censuses.

Table 3

Housing Inventory, Tenure and Vacancy
Sioux Falls, South Dakota MSA
1990 and 2000

	April 1990	April 2000
Total Housing Inventory	55,603	69,368
Occupied Housing Units	53,142	66,778
Owner Occupied	34,021	44,507
Percent	64.0%	66.6%
Renter Occupied	19,121	22,271
Percent	36.0%	33.4%
Vacant Housing Units	2,461	2,590
For sale	360	481
Owner Vacancy Rate	1.0%	1.1%
For Rent	1,060	1,475
Renter Vacancy Rate	5.3%	6.2%
Other Vacant	1,041	634

Source: U.S. Bureau of the Census

The increase in the local homeownership rate was a significant housing inventory change in the past decade, although it lagged the rest of the state. The Sioux Falls MSA homeownership rate is the higher of the two metro areas in the state and above the rate for the U.S. (66.2 percent), but below the state of South Dakota (68.2 percent). The Minnehaha County portion (64.7 percent) of the MSA ranked among the lowest (53rd of 66) for all counties, but among the highest in the increase in homeownership (24th of 66) from 1990 to 2000. In contrast, the Lincoln County portion (79.7 percent) ranked among the highest (9th of 66) for all counties, but among the lowest (20th of 66) for the increase during the decade. The Sioux Falls MSA accounted for nearly 45 percent of South Dakota's increase in total housing units, including about 70 percent of the state's increase in renter occupied units during the past decade. This indicates the continued dominance of the MSA as the primary economic and population center of the state.

Residential Building Trend

The strong economy has stimulated residential building. The number of new single-family units permitted during the 1990s set a decade record by more than doubling the level of the previous decade. In 2000, record production continued, surpassing the previous high recorded in 1999 by nearly 15 percent. The trend in new construction permits is presented in the following table.

Table 4

Housing Units Authorized by Building Permits
Sioux Falls, South Dakota MSA
1990 - 2001

Year	Single Family (a)	Multifamily (b)	Total
1990	530	202	732
1991	710	581	1,291
1992	874	283	1,157
1993	847	684	1,531
1994	901	850	1,751
1995	830	688	1,518
1996	1,033	514	1,547
1997	1,138	218	1,356
1998	1,323	293	1,616
1999	1,428	406	1,834
2000	1,556	749	2,305
Jan-Jun 2000	786	409	1,195
Jan-Jun 2001	768	136	904

(a) Single-family permits include all structures of one unit and townhouses. This excludes manufactured homes placed on foundation or pads (estimated to be about 600 units in total since 1990).

(b) Multifamily permits include all structures with 2 or more units (including condominiums).

Source: U.S. Bureau of the Census; Sioux Falls Planning and Development Services

Single-family building slightly slowed in 2001; from January through June, the number of new units permitted declined by 2.3 percent from last year's level during the same time period. Unusually cold weather and a slower economy put a slight damper on single-family production this year. New homes make up about 30 percent of the sales market in Sioux Falls. The city accounted for the vast majority permit activity in the MSA, with much of the activity located in the south part of the city where most of the available land is located. According to Prudential Chell REALTORS, approximately 60 percent of the new homes sold through June of this year are priced below $150,000 or close to the South Dakota Housing Development Authority's (SDHDA) price limit for first time homebuyers of $141,012. The move-up range of $150,000 to $200,000 was the next most popular with 30 percent of new homes, while high-end homes priced above $200,000 made up the balance. Since 1990, Sioux Falls city portion of the MSA's total single-family construction held at a steady 90 percent.

Multifamily building also set a record for the decade, but varied considerably from year to year. Approximately 60 percent of the decade total of 5,000 units was built in the mid-1990s. During the cutback period in the late-1990s, construction shifted from a preponderance of tax credit to a more moderate level of market rate units. As the rental market improved, another construction surge occurred in 2000 when approximately 750 multifamily units (600 apartment) were started, nearly all of which were market-rate. The market has already absorbed 450 of the apartment units. The remaining 150 apartment units will be finished this summer or early fall, while the balance of 150 multifamily units is a combination of condominiums, elderly congregate or duplex/twin homes units. Through June of this year, permits have been issued for only about 140 multifamily units, including about 100 apartment units. These will come on line by this winter. Also, expected to start construction this year are another 335 units in six apartment projects, including three market-rate and three LIHTC projects.

Since 1990, nearly 5,000 units in over 100 apartment projects have opened or are under construction. There are six projects currently under construction; all are in Sioux Falls (one LIHTC and five market rate). In total, there are about 250 apartment units (excluding a small number of duplexes and condominiums) under construction.

As mention above, the pipeline of projects not yet under construction but in the late planning stages includes 335 units in six projects. All of these are in Sioux Falls and are a mix of market rate and family LIHTC projects. Of the three market rate projects, two are additions to existing complexes and the third will be townhouse design with attached garages. The three LIHTC family projects are primarily aimed at households earning 50 and 60 percent of area median income. These projects are also of two and three bedroom townhouse design. There are very few projects in early planning stages; when and if additional projects will start construction is unknown at this time.

The only LIHTC projects completed over the past few years are the 30-unit Westpointe I Apartments and the 44-unit Bergeland elderly apartments. The largest recently built market rate apartment complexes range from the 32 units at the most recent phase at Royal Oaks to 144 units at Lexington Estates.

Present Multifamily Construction Activity

The six projects currently under construction are described below:

Lexington Estates, 144 units :

This project is located in southwest part of the city off of Marion and 51st street. It is a secured entry building with all two and three bedroom market rate units. Amenities include a washer/dryer in each unit, heated indoor/outdoor pool, exercise room and heat is included in the rent. The first two buildings opened in June, while the 48-unit third building is expected to be open this summer.

Westpointe I, 30 units:

Located in northeast Sioux Falls, the site is located just off the Interstate 229 and Benson Road interchange. The first buildings of this townhouse project opened in July and the last one should be completed by August. All of its two and three bedroom units will be income restricted to households earning between 50 and 60 percent of area median income. Amenities include a central air conditioning, washer/dryer in each unit, playground and off-street parking.

Platinum III, 66 units:

This is a third phase of an existing 132-unit apartment project in southwest Sioux Falls near 69th and Louise. The market rate project includes patios/balconies, washer/dryer hookups, pool and community room. The building should be finished by September 2001; a fourth phase should begin sometime this fall or winter.

Royal Oak II, 32 units:

This is a phase II addition to an existing 120-unit market rate project in southwest Sioux Falls. Located off of 49th and Oxbow, the first phases of the project were built in the early 1990s. Amenities include indoor pool, Jacuzzi, exercise room, unit washer/dryer and under building parking. Construction of this phase should be completed by winter.

Meadowbrook II, 40 units:

This is a second phase addition to an existing 32-unit market rate project in southwest Sioux Falls. Located off of 12th and Lyons Boulevard, the first phase of the project opened last year. Amenities include off street parking and deck/patio in each unit. Construction of this phase should be completed by fall of this year.

Harr Apartments, 48 units

Located off of 41st and Sycamore, this market rate project started construction this summer. Amenities include off street parking and deck/patio in each unit. Construction should be completed by winter.

In total, there are approximately 250 apartment units still under construction; about 90 percent are market rate units while 10 percent are LIHTC units. About 40 percent of the units should be coming on line by this summer or early fall, while the remaining units by late this year or early next year. The market should be able to absorb this level of building.

Proposed Multifamily Construction Activity

Projects likely to start construction within the next several months include three LIHTC and two market rate projects. These are described below:

Westpointe II, 42 units:

The site is located in northeast Sioux Falls. This second phase is expected to begin construction this fall. All of its two and three bedroom units will be income restricted to households earning between 50 and 60 percent of area median income. Amenities include a central air conditioning, washer/dryer in each unit, playground and parking.

Stoney Creek, 60 units:

Located in southwest Sioux Falls off of Sertoma and Stoney Creek. This townhouse project is expected to begin construction this fall. All of its two and three bedroom units will be income restricted to households earning 60 percent of area median income. Amenities include a central air conditioning, washer/dryer in each unit, playground and off-street parking.

Brennan Hill, 59 units:

Located in northeast Sioux Falls, the site is just off of Sycamore and Brennan Drive. This townhouse project is expected to begin construction by this fall. All of its two and three bedroom units will be income restricted to households earning 60 percent of area median income. Amenities include a central air conditioning, washer/dryer in each unit, playground and off-street parking.

Sunnycrest Village III, 60 units:

This project has applied for HUD/SDHDA financing and is located near 41st and St. James in northwest Sioux Falls. The addition will be the third phase of an existing 108-unit mixed income (Section 8 and market rate) elderly project. All of the new units will be market rate and construction is expected to begin this fall. Project features include expanding the existing community room and underground parking.

Platinum IV, 66 units:

This is a fourth phase of an existing 132-unit (plus another 66 units under construction) apartment project in southwest Sioux Falls located near 69th and Louise. The market rate project includes patios/balconies, washer/dryer hookups, pool and community room. The building should begin construction this fall or winter.

57th and Sertoma Apartments, 48 units:

Located in southwest Sioux Falls, this project should begin construction this summer or fall. All its units are market rate and of two bedroom, one bath design. Amenities include off street parking, deck/patio, washer/dryer hookups and garages in the rent.

In total, there are 335 units in the six apartment projects in the late planning stage. Of the 335 units, 161 are in three LIHTC projects. The vast majority of these units (146) are income restricted to households earning less than 60 percent of area median income, while the remaining 15 are at the 50 percent level. There are 174 units in the three market rate projects.

Home Sales Market

The trend since 1996 is presented in the following table (complete data for the MSA is not available prior to 1996):

Table 5

Existing Single Family Sales
Sioux Falls City, South Dakota
1996 - 2001

Year	Number of Sales	Average Sales Price	Percent Change	Ending Inventory
1996	1,713	$102,495	na	409
1997	1,697	$108,754	6.1%	400
1998	1,901	$111,061	2.1%	415
1999	1,863	$123,421	11.1%	328
2000	1,719	$124,441	0.8%	429
June 2000(a)	820	$123,006	na	375
June 2001(a)	804	$129,157	5.0%	513

Source: Prudential Chell REALTORS; Sioux Falls Board of REALTORS

Sioux Falls' existing home sales market is currently balanced despite a build up in inventory. The average existing single-family sales price increased by 5 percent to $129,200 from January through June 2001 compared to the same time period in 2000. Sales activity during this period slightly declined, while inventory is up significantly from one year ago.

Some price ranges are stronger than others. Homes priced under the SDHA existing purchase price limit $111,412 are in short supply, while there is more availability for homes priced up to $140,000 because of competition from new construction. At the same time, homes priced under $85,000 take longer to sell because of the potential for needed repairs. Higher priced homes of over $250,000 also face competition from new construction. Homes sold in the city represent about 70 percent of all activity in the MSA and prices are approximately 10 percent higher than in the rural areas of the MSA. Last year, FHA financing was used for approximately 30 percent of all existing single-family sales. A significant build up of inventory (up by over 30 percent) over the past few years could portend some weakening of the market during the second half of 2001.

Rental Market Conditions

Rental market conditions have improved from the overbuilding of the 1993 to 1996 time period, including the market for tax-credit projects. The average overall vacancy rate declined from nearly 10 percent recorded in 1996 to below 5 percent over the past few years (see table 5 below).

The market improved because of a major cutback in construction in 1997 and 1998 accompanied by strong rental household growth. The tax credit market took longer to stabilize because of the preponderance of tax credit units that were built in the mid-1990s and the high capture rates needed to achieve sustaining occupancy. As the rental market improved, another construction increase occurred in 2000 when approximately 750 multifamily units were started. Because of the number of units coming on line this year, the vacancy rate increased during the first quarter of 2001 to a still balanced 4.8 percent. Despite the vacancy rate increase, small rent increases are common and most concessions have been eliminated. The average two-bedroom first quarter 2001 conventional rent increased to $556 or up by 4.1 percent from 2000 and 9.4 percent from 1999. The average two-bedroom tax credit rent of $501 was up 1.2 percent from last year.

The trend in apartment vacancy rates from a survey begun in 1997 is shown in the following table:

Table 5

Apartment Vacancy Rates
Sioux Falls, South Dakota MSA
1997 - 2001

	Vacancy Rates		
Survey Date	Overall	Conventional	Tax Credit
1st Quarter 1997	9.7%	9.9%	10.2%
3rd Quarter 1997	5.2%	5.0%	6.8%
1st Quarter 1998	6.8%	6.4%	10.6%
3rd Quarter 1998	5.4%	4.9%	9.6%
1st Quarter 1999	5.9%	6.1%	4.0%
3rd Quarter 1999	3.3%	3.1%	5.8%
1st Quarter 2000	3.4%	3.2%	4.9%
3rd Quarter 2000	2.9%	2.7%	4.9%
1st Quarter 2001	4.8%	4.7%	5.1%

Source: South Dakota Multifamily Housing Association

Recently opened larger apartment projects have been leasing up well at two-bedroom rents from $750 to $850, excluding heat. Many of the newer projects offer a considerable amenity package, including underground heated parking, washers and dryers in each unit, exercise, swimming pool and computer rooms. In general, projects that have come on line over the past year have leased-up quickly without the use of major concessions.

We expect the market to remain balanced during the second half of 2001 and begin to slightly tighten by the first half of 2002. The approximately 250 units under construction are spread out reasonably well with completion times scheduled for this fall or winter. The market should absorb these without any major adjustments. There are only a few projects in the late planning stages and, coupled with an overall cutback in production this year, the market should begin to firm during the first half of 2002. An improved economy and continued in-migration will increase demand for rental units in 2003.

Household Growth and Renter Demand Forecast

During the 1990 through July 1, 2001 time period, building permits were issued for about 17,500 units in the Sioux Falls MSA. The great majority of these (about 11,900 units) were single-family homes and townhouses. Of the remaining 5,600 multifamily units, we estimate that nearly 5,000 were actually in rental projects. Owner occupied condominiums and duplexes account for the balance of multifamily units permitted. The absorption of the new rental units and a slight increase in renter vacancies resulted in an average absorption of about 400 rental units per year since 1990.

Single-family construction activity resulted in some shift to homeownership in the area. We estimate that the homeownership rate rose from about 64 percent in 1990 to nearly 67 percent at the present time. Even with some continued small shift to homeownership, rental demand will remain close to the average annual production level during the 1990s.

We estimate that future employment gains of 2.75 percent for the first year and 3 percent for the second year will generate average household growth of nearly 1,700 households per year. The number of households will increase by approximately 1,600 households in 2002 and by 1,800 households in 2003. After adjusting for tenure shift, units under construction and mobile home impact, this level of growth should support production of 400 rental units in 2002 and 500 in 2003 or an average of 450 units a year. This is near the average annual production level since 1990 of about 500 rental units a year.

There is some risk to these forecasts in the short run. Recent migration has continued at the level typical of the past few years, while employment growth has slowed. This migration has propped up the housing market, which could be vulnerable if employment growth does not pick up and discouraged job seekers leave the area and/or potential workers from outside the area delay plans to relocate to Sioux Falls. However, given the positive outlook for Sioux Falls, we expect employment growth to catch up to the continued flow of in-migrants by late 2001, helping to avert a major adverse impact on the housing market.

At present, there are about 250 rental units under construction in six projects (discussed earlier); these are expected to come on line over the next several months. This level of construction is below the expected first year absorption level. There are approximately 550 in various stages of planning. Of this total pipeline, there are 335 units in projects actually expected to begin construction in the next several months. The balance of pipeline projects (containing about 200 units) is in the early development stage; when and if they begin construction is unknown at this time.

About half of the 335 units in late planning, but not yet under construction, are LIHTC units. The presence of below market rents normally would boost rental absorption in the short run above the level one would expect if all were market rate, general occupancy projects. However, absorption of these units will require pushing 60 percent capture rates, especially for the three bedroom units, to the upper limits. These projects will take longer to lease-up or may lease-up be at the expense of other projects. The limited number of market rate units in the immediate pipeline leaves some opportunity for this type of product now and over the next few years. Starts could begin this year with units coming on line during the first half of 2002 or starts could wait until any time in 2002 with units coming on line during the second half 2002 or first half of 2003. This level and timing of construction will keep the rental market in balance over the next two years. Mixed income, with a 40 percent LIHTC component, and/or class B product would be well received at any time during the next two years. One and four bedroom units are also in short supply for all income levels. There is also need for elderly LIHTC units at all income levels.

Household Growth and Owner Demand Forecast

We estimate the demand for owner occupied units at about 1,275 units a year over the next few years. The 2002 demand is 1,200 units and as economic growth increases in 2003, demand increases to 1,350 units. Most of these units should be single-family detached homes, although we expect that 10 percent of the demand will be met by manufactured homes in parks (and lots), townhouses, duplexes and condominiums. The proportion of townhouses and condominiums has crept up over the past few years.

Subsidized Housing

There are about 1,200 units in HUD subsidized projects in the Sioux Falls MSA. Nearly all of these are covered by Section 8 housing assistance payments contracts. This subsidy typically allows tenants to pay 30 percent of their income for rent. Participation in the Section 8 program is generally limited to households with incomes less than 50 percent of the median income for the Sioux Falls MSA. At present, this income limit is $28,850 for a family of four and $20,200 for an individual. Just about two thirds of the total HUD-subsidized inventory is in projects for the elderly. With few exceptions, these projects are full, experience low turnover and have waiting lists, especially in Sioux Falls city. The nonelderly projects also maintain waiting lists but are more likely to have vacancies at any given time due to the considerably higher turnover in these units. Conversely, elderly projects outside the Sioux Falls commuting area have difficulty maintaining full occupancy. Many of these smaller, more remote communities have experienced a loss of population and employment to the more urbanized areas of the state, including Sioux Falls.

The Sioux Falls Housing and Redevelopment Commission (SFHDC) manages most of the 1,700 Section 8 Vouchers used in the Sioux Falls Metro Area;. These are issued to eligible tenants who find their own units in the market and contribute 30 percent of their income for rent. Eligibility for vouchers is also limited to households with incomes less than 50 percent of the median but three-fourths of vouchers are targeted to households with incomes less than 30 percent of the median ($17,100 for a family of four, $12,100 for an individual). Utilization of vouchers is high and the SFHDC maintains a waiting list of almost 800 households, including about 300 elderly. Nearly all these households are seeking the use of Section 8 vouchers since the local housing authorities manage few individual projects. We estimate there are about 5,000 renter households in the Sioux Falls MSA with income less than 50 percent of the median and paying more than 30 percent of income for rent. There remains a large unmet need for rental assistance in the Sioux Falls MSA, but primarily in the Sioux Falls city area.

Low Income Housing Tax Credit (LIHTC)

The tax credit market has taken a few years to recover from the overbuilding of the 1993 to 1996 period. It is now balanced after an extended adjustment period, but at rents far below the maximum allowable under the program. The slow recovery was the result of too many new units targeting the same income group and coming on line within a relatively short period of time. There have been few units produced during the past three years. This cutback, along with an improved general market, has helped the LIHTC market recover. Amenities for these projects compete very well with the general market, and rents are approximately $50 to $100 below comparable market rate projects. Project owners have kept their rents well below the maximums permitted by the program. Rents, even at the 60 percent of income level, are below the present Section 8 Fair Market Rents and below the 50 percent maximum rent. A significant increase in income limits for FY 2001 has also helped the tax credit market. The two and three bedroom 50 and 60 percent market is competitive because of the concentration of units at those income levels

The present inventory of 1,220 LIHTC units (including 130 elderly) entered the market beginning in the late 1980s. In the immediate pipeline are nearly 300 LIHTC units in five projects, all located in Sioux Falls city. These are predominantly 60 percent two and three bedroom units. Four of the projects have been described earlier; one is under construction, while the remaining three are expected to start this fall. The fifth project, Elmwood Estates, is an existing 98-unit market rate project that will undergo substantial rehabilitation with FHA financing. The project has already received tax credit allocation for all of its units at the 60 percent income level.

Market Potential for Nonelderly LIHTC Units

The market potential for LIHTC units consists of households that are both income qualified and can afford the proposed rents. Table 6 illustrates the maximum incomes by bedroom size (assuming 1.5 persons per bedroom), maximum shelter rents (30 percent of the maximum income limit less a utility allowance) and estimated minimum incomes (assuming a typical requirement that tenant income be at least 2.5 times monthly shelter rent) at the 40, 50 and 60 percent of income level. As mentioned earlier, actual tax credit rents are considerably below the maximum allowable under the program. Therefore, we have also shown the minimum incomes needed to afford these lower rent levels; households within these income ranges form the target market for any given project and/or units at that income level. For example, the target income level for a 60 percent two-bedroom unit would be for households with incomes ranging from $18,000 to $31,140. These computations are based on Fiscal Year 2001 income limits for the MSA that were effective April 6, 2001. The utility allowances have been estimated by the SFDHC.

The following table shows income levels, maximum shelter rents and actual rents under the LIHTC program:

Table 6

Target Resident Incomes and Rents by Bedroom Size
Sioux Falls, South Dakota MSA
Fiscal Year 2001

40 Percent of Median Income (a):	Number of Bedrooms			
	One	Two	Three	Four
Maximum annual income	$17,320	$20,760	$24,000	$26,760
Maximum monthly shelter rent	$381	$452	$521	$669
Minimum annual income	$11,430	$13,560	$15,630	$17,190

50 Percent of Median Income:	Number of Bedrooms			
	One	Two	Three	Four
Maximum annual income	$21,650	$25,950	$30,000	$33,450
Maximum monthly shelter rent	$541	$649	$750	$836
Minimum annual income	$14,670	$17,460	$20,130	$22,200
Estimated actual shelter rent	$400	$500	$600	$700
Minimum annual income	$12,000	$15,000	$18,000	$21,000

Table 6 (continued)

60 Percent of Median Income:	Number of Bedrooms			
	One	Two	Three	Four
Maximum annual income	$25,980	$31,140	$36,000	$40,140
Maximum monthly shelter rent	$650	$779	$900	$1,004
Minimum annual income	$17,940	$21,360	$24,630	$27,240
Estimated actual shelter rent	$500	$600	$700	$800
Minimum annual income	$15,000	$18,000	$21,000	$24,000

(a) There are no existing 40 percent units in the MSA.

To estimate the potential market in each range, we updated 1990 Census data that presented incomes by household size and tenure for all households. We assumed a faster growth in these target renter households than in total renters since some shift to homeownership has lowered the proportion of higher income renters. Consequently, the proportion of lower income renters has increased more than the total. Households were allocated to bedroom sizes based on occupancy patterns derived from the American Housing Survey. By comparing the above income ranges to the updated income distribution, we computed the number of renter households in each range. We then compared this to the number of units for this target group to obtain capture rates. Since Section 8 vouchers account for approximately 40 percent of current residents, we have also adjusted the number of existing units by this factor. Because the bulk of projects under construction or proposed are likely to exceed the FMRs, we have lowered this adjustment factor to 20 percent. Also, the number of vouchers in the MSA has been constant for the past several years and may not be as available for new projects.

The results of this analysis are presented below in table 7. Note that we have derived two sets of capture rates for each income level. The first is based only on completed units in the present inventory. The second is derived from the total of completed, under construction and proposed units. This later computation tells us the capture rates the LIHTC market will have to achieve to successfully absorb all units presently under construction and proposed. Both sets of capture rates have been adjusted to reflect tenants expected from outside the market area, estimated to be approximately 20 percent.

Table 7

Nonelderly Market Potential and Capture Rates
Sioux Falls, South Dakota MSA
July 2001

40 Percent of Income:	One	Two	Three	Four	Total
	Number by Bedroom Size				
Total Renter Households	8,610	6,220	2,550	910	18,290
Targeted Renter Households	810	540	240	100	1,690
Completed units	0	0	0	0	0
Adjusted Capture rates:	**na**	**na**	**na**	**na**	**na**
Complete, under constr., proposed	0	0	0	0	0
Adjusted Capture rates:	**na**	**na**	**na**	**na**	**na**

50 Percent of Income:	One	Two	Three	Four	Total
	Number by Bedroom Size				
Total Renter Households	8,610	6,220	2,550	910	18,290
Targeted Renter Households	1,640	870	420	160	3,090
Adjusted completed units	4	38	31	1	74
Adjusted Capture rates:	**0.2%**	**4%**	**6%**	**1%**	**2%**
Completed, under constr., proposed	4	48	40	1	93
Adjusted Capture rates:	**0.2%**	**4%**	**8%**	**1%**	**2%**

60 Percent of Income:	One	Two	Three	Four	Total
	Number by Bedroom Size				
Total Renter Households	8,610	6,220	2,550	910	18,290
Targeted Renter Households	2,140	1,190	580	220	4,130
Adjusted completed units	59	259	264	5	587
Adjusted Capture rates:	**2%**	**17%**	**36%**	**2%**	**11%**
Completed, under constr., proposed	85	364	346	5	853
Adjusted Capture rates:	**3%**	**25%**	**48%**	**2%**	**16%**

Note: Capture rates adjusted 20 percent for out of area tenants. Completed units adjusted by 40 percent factor for Section 8 voucher tenants; proposed and under construction units adjusted by 20 percent factor.

Source: Estimated by HUD Economist

The total capture rates achieved for completed units are modest for the 50 percent target group, ranging from 0.2 to 6 percent. However, these rates are misleading since there is considerable overlap with the 60 percent market (see discussion in paragraph below). There are no existing or proposed 40 percent units in the market area. For the 60 percent target group, the overall capture rate of 11 percent, although still reasonable, is considerably higher than that for the 50 percent group. With the exception of the 60 percent three-bedroom rate, these rates are consistent with the generally balanced state of the present LIHTC market. Because the vast majority of units in the pipeline are 60 percent units, the two and three bedroom rates increase dramatically. Capture rates increase from 17 to 25 percent for the two bedroom and 36 to 48 percent for the three bedroom units. There are no units proposed at the 40 percent level or four bedroom units at any income level.

There can be considerable overlap between various income levels. For example, a family needing a two-bedroom unit with an income of $21,650 can afford the minimum rent in a 60 percent unit but is below the maximum income limit for a 50 percent unit (refer to the income levels in Table 6). Since there is such a large overlap, we have produced estimated 50 and 60 percent capture rates for these units in the aggregate. These results are presented in Table 8.

Table 8

Nonelderly Market Potential and Capture Rates
Sioux Falls, South Dakota MSA
July 2001

	Number by Bedroom Size				
50 & 60 Percent of Income:	One	Two	Three	Four	Total
Total Renter Households	8,610	6,220	2,550	910	18,290
Targeted Renter Households	2,540	1,410	670	240	4,860
Adjusted completed units	63	298	284	6	651
Adjusted Capture rates:	**2%**	**17%**	**34%**	**2%**	**11%**
Completed, under constr., proposed	96	441	397	6	940
Adjusted Capture rates:	**3%**	**23%**	**45%**	**2**	**15%**

Note: Capture rates adjusted 20 percent for out of area tenants. Completed units adjusted by 40 percent for Section 8 voucher tenants. Proposed and under construction units adjusted by 20 percent factor for Section 8 voucher tenants.

Source: Estimated by HUD Economist

These estimates show that the capture rates decrease (from Table 7) for the 60 percent two and three bedroom units when including all 50 percent renter households and the 50 percent units. This indicates that the actual 60 percent rents are low enough to target a significant number of 50 percent households, while, at the same time, there are very few completed or proposed 50 percent units. Despite the lower 50/60 percent capture, the rates for the two and three bedroom units significantly increase, while the three bedroom rate is at a very high level.

Establishing attainable capture rates is imprecise but in view of increasing market rents, growth in the Sioux Falls area and past experience, we anticipate that the market could exceed the 30 percent level at this time. However, a longer than normal adjustment period could take place as it did following the construction surge of the mid-1990s. Rents for some projects may need to be lowered to attain the higher capture rates, especially the three-bedroom units. The underserved 40 percent market is well below this level as are one and four bedroom for all income levels. The two-bedroom 60 percent market, while the increase is significant, remains slightly under 30 percent. Conversely, the 60 percent three-bedroom market must attain a level that has not been seen in any of our market areas. The use of Section 8 vouchers in tax credit projects is unlikely to increase dramatically because of the relatively constant number of vouchers in the market area. Over the long term, as the LIHTC and market rents begin to diverge, capture rates could go higher. In the short term, development should be directed towards the 40 percent market for all unit types, and at the 50 and 60 percent one and four bedroom markets.

In summary, there is considerable potential for developing additional LIHTC units at the 40 percent level for all unit types, and the 50 and 60 percent level for the one and four bedroom markets. Of course, there is demand from families who cannot afford the minimum rents at typical levels of LIHTC units without additional subsidy such as Section 8. The vast majority of Section 8 voucher recipients in the area have incomes less than $12,000, an income group unable to afford the 50 or 60 percent LIHTC units. The two bedroom 60 percent capture rate will be pushed considerably higher after completion of units proposed but the three-bedroom rate will be at a level that has not been tested in our market areas. Following the completion of the proposed tax credit projects, we expect some adjustment period to return to balanced conditions. Therefore, we encourage more production emphasis on all 40 percent unit types and 50 and 60 percent one and four bedrooms, while the two and three bedroom 50 and 60 percent production could wait until the market stabilizes.

Market Potential for Elderly LIHTC Units

There are numerous subsidized elderly housing projects for very low-income households (50 percent of median income) in the MSA that were developed under the Low Rent Public Housing program or the Section 8 program. While there is some overlap with the LIHTC market, it is very small because tenant incomes in these projects are usually too low to afford the tax credit rent. Very low-income elderly households can use vouchers in LIHTC projects.

There has been some development of elderly LIHTC projects in Sioux Falls. Four projects containing 132 units were built during the later half of the 1990s. Seventy percent of these units were developed at the 60 percent of income level, while the balance is made up of 50 percent units. All of the units are of one-bedroom design. The elderly tax credit market is strong; projects are full and most maintain waiting lists. The newest project, the Bergland Apartments, leased up quickly. These projects are presented in Table 9.

Table 9

Income Targets, Bedroom Distribution and Status of Elderly LIHTC Projects
Sioux Falls, South Dakota MSA
July 2001

Completed:

	One bedroom			Two bedrooms			
	40	50	60	40	50	60	Total
Bergland		20	24				44
Gateway			23				23
West Creek		17	24				41
Western Comfort			24				24
Total	**0**	**37**	**95**	**0**	**0**	**0**	**132**

Proposed:

	One bedroom			Two bedrooms			
	40	50	60	40	50	60	Total
Western Heights.		50					50
Grand Total	**0**	**87**	**95**	**0**	**0**	**0**	**182**

The potential market for these units is estimated using a methodology similar to that discussed in the previous section dealing with the nonelderly LIHTC market. The minimum incomes are equal to those in the previous section (see Table 7) but the maximum limits are the one and two person income limits for the appropriate level. The total potential below includes both one and two person households. Our experience indicates that about 80 percent of elderly LIHTC one-person households occupy units. The capture rate shown has been adjusted to reflect this. For example, the 95 units that exist at the 60 percent level will have to rent to about 80 one-person households to be absorbed (.80 times 95). Also, based on past experience, approximately 10 percent will be occupied by out of area tenants, resulting in a need to capture approximately 70 single persons in the local market. The inclusion of a portion (approximately 10 percent) of homeowners also lowers the number of single persons to about 60 persons.

The homeowner factor is more relevant for the 60 percent units because persons in this income group are more likely to own a home than those at the 40 and 50 percent levels. The adjusted capture rate of 7 percent represents the proportion of eligible single person households represented by these 60 persons. In this case, we have not adjusted for voucher holders since the capture rates are very modest. The results for the 40, 50 and 60 percent of income group are shown in Table 10.

Table 10

Elderly Market Potential and Single Person Renter Capture Rates
Sioux Falls, South Dakota MSA
July 2001

40 Percent of Income:	Total
Total Elderly Renter Households	4,060
Targeted Elderly Renter Households	770
Completed	0
Adjusted capture rate:	na
Completed, under constr., proposed	0
Adjusted capture rate:	na
50 Percent of Income:	Total
Total Elderly Renter Households	4,060
Targeted Elderly Renter Households	1,070
Completed	37
Adjusted capture rate:	**2%**
Completed, under constr., proposed	87
Adjusted capture rate:	**5%**
60 Percent of Income:	Total
Total Elderly Renter Households	4,060
Targeted Elderly Renter Households	900
Completed	95
Adjusted capture rate:	**7%**
Completed, under constr., proposed	95
Adjusted capture rate:	**7%**

The total capture rates achieved for the completed units are low for the 50 and 60 percent units and no 40 percent units have been produced. These rates are consistent with the strong state of the present elderly LIHTC market. We have not adjusted for the possibility that some of these targeted households are already being served in subsidized units but a majority of the Section 8 subsidized elderly residents in the MSA have incomes under $10,000, below all minimum incomes. This would only marginally impact the 40 and 50 percent LIHTC capture rates. Also, adjusting for the use of Section 8 vouchers in existing projects would also lower capture rates. The only proposed elderly project (Western Heights) is a 50 percent project that has not received tax credit allocations from the SDHDA. However, we included the project to illustrate its impact following completion; the 50 percent capture rate increases to a very small 7 percent. In view of the modest capture rates in this segment of the market, there is some potential to develop elderly LIHTC units at all income levels.